Debt Versus Savings, Which Comes First?

Which came first the Chicken or the Egg? Another interesting question is... What's more important, to pay off debts or save first? When you think about the issue of paying down debt before saving money, it's important to take a step back and consider the big picture.

A Different Approach

When you start out in life you establish credit by utilizing credit cards, auto loans & student loans. You typically have very little savings. So when life's emergencies and events occur you usually turn to the only place you have available, credit cards and personal loans. Imagine if you took a different approach? One we advocate for within The Living Balance Sheet®.

What if you focused on using your first dollars to protect your income and protect against unexpected life events? Examples include car accidents, law suits, illness, death, disability. Next you could focus on saving 15% to 20% of gross income and build up a year's income in savings. Then you can begin to pay down the non deductible debt and all debts after that. This is opposite the approach advocated by many financial representatives which is to begin paying all debts without protection from life's events, and without regard to having a good savings discipline first. It is this thinking that may have contributed to Americans having high credit card debt and student loan debt. Then when an unexpected event occurs and adequate savings is not in place, the debt increases.

The cycle of building up debt and paying it down, only to build it up again, is so prevalent in today's society that many Americans live their entire life with this cycle repeating itself.

So, consider starting today by putting your future ahead of the credit card companies and banks. Commit to protect your most valuable asset, which is you and your ability to earn an income. Give proper attention to maximum auto, home and umbrella coverages. Then, commit to save a minimum of 15% to 20% of your gross income and consider building savings of one year of gross income in liquid accessible funds. Do not count your 401(k) in this equation as it should not serve as a short term savings account. There are restrictions on withdrawals under the age of 59&1/2 including penalties and taxes. Lastly, work on paying off credit cards, auto's and other non-deductible debts.

It's okay to be different than the majority of Americans when it comes to this issue. Different can translate into a sound strategy and future.

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